MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2022/2023

BAC 3624 – ADVANCED AUDITING

(All sections/Groups)

11 JULY 2023
9.00 a.m – 12.00 p.m
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of 7 pages with 5 questions only.
2. Attempt **ALL** questions. The distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided.

QUESTION 1

(a) Your firm is the external auditor of Aman Berhad (Aman), a listed company. The directors of Aman have requested that your firm helps in the preparation of its annual financial statements.

Required:
Explain the threats to your firm's objectivity arising from the above and describe the safeguards, if any, which should be put in place to mitigate those threats.

(4 marks)

(b) The ICAEW Code of Ethics identifies circumstances where an auditor is or may be required to disclose, to third parties, confidential information obtained during the course of an external audit.

Required:
List, with examples, the circumstances in which the disclosure of confidential information, without the client's permission, is or may be required.

(4 marks)

(c) Your firm is the external auditor of Mapel Berhad (Mapel) for the year ended 30 July 2023. On 15 July 2023, the directors of Mapel engaged a firm of expert property valuers to provide an independent valuation of the company's freehold land and buildings. The directors intend to recognise freehold land and buildings at this valuation in the financial statements for the year ended 30 July 2023.

Required:
State the audit procedures that your firm should plan to undertake to determine whether the valuation provided by the firm of expert property valuers can be used.

(3 marks)

(d) The risk of management override of internal controls is present in all audited entities.

Required:
Explain three audit procedures that should be included in external audit plans to address this risk. (3 marks)

(e) Your firm recently conducted the external audit of the financial statements of ABC Berhad (ABC) for the year ended 28 February 2023. ABC's bank requested the audited financial statements before deciding whether to make a loan to ABC. ABC received the loan from its bank but has defaulted on its first quarterly loan repayment. Your firm's audit report was unmodified.

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Required:
In respect of the bank has relied on the audited financial statements, explain the possible consequences for your firm if it has provided an inappropriate opinion in the auditor's report on ABC's financial statements. (4 marks)

(f) You are the audit junior working on the external audit of Bina Sdn Bhd (Bina). The sales ledger clerk informed you that when he requested the payment of an overdue amount from Mr Anju, a sole trader, he was told by Mr Anju that the managing director of Bina had personally collected the overdue amount in cash. The managing director subsequently instructed the sales ledger clerk to write off the overdue amount as a bad debt. The amount is not material to the financial statements.

Required:
State with reasons, the actions that should be taken by you and your firm in relation to this matter. (2 marks)

(Total: 20 marks)

QUESTION 2

Energy Solar Malaysia Sdn. Bhd.

Energy Solar Malaysia Sdn. Bhd. (ESM) has been an external audit client of your firm for 10 years. The principal activity of the company is the provision of design and installation services for quality solar systems at any business and personal premises. Alex has acted as the engagement partner for the last 8 years and Alya has acted as the audit manager for the last 5 years.

While planning the audit of ESM for the year ended 31 July 2023, Alya was taken ill and you have been assigned to replace her. You have not worked on the ESM audit before. On reading the background information you ascertain the following:

- All work performed by the company is carried out under short-term, fixed price contracts for customers in Malaysia. ESM's staff design the systems to customers' specifications and then procure the components from suppliers based outside Malaysia, mostly from China and Taiwan. These suppliers invoice ESM in their own local currency.

- The contract price is negotiated and agreed with the customer before commencement of work. The terms of payment require an initial payment of 30% of the contract value before the commencement of any work and the balance to be paid on the successful installation of the system.

Continued ...

- Each contract has a project manager who is responsible for monitoring costs against budget. All direct costs relating to each contract are recorded in the company's job costing system which is integrated with the purchases and payroll system. The finance director uses the cost records to calculate the value of work in progress for the monthly management accounts and the year-end financial statements. Provision is made for contract losses where appropriate.

Before she fell ill, Alya had prepared the audit strategy but not the audit plan. The audit strategy identifies the following as key areas of audit risk:

1. Revenue
2. Work in progress
3. Trade receivables
4. Going concern

The strategy also includes the following extracts from the financial statements:

Statement of profit or loss

	Years ended 31 July	
	Draft 2023 (RM'000)	**Actual 2022 (RM'000)**
Revenue	27,851	24,687
Purchases (components)	(8,802)	(8,879)
Gross profit	5,879	4,448
Profit from operations	1,493	1,486
Finance cost	(961)	(689)

Statement of financial position (balance sheet)

	As at 31 July	
	Draft 2023 (RM'000)	**Actual 2022 (RM'000)**
Current assets:		
Work in progress	2,522	1,906
Trade receivables *(Note 1)*	5,276	4,012
Non-current liabilities:		
Borrowings:		
Bank loan	2,500	3,000
Director's loan	500	-
Current liabilities:		
Trade payables	1,162	1,301
Other payables *(Note 2)*	1,445	966
Borrowings:		
Overdraft (facility RM4 million)	3,999	3,828
Bank loan	500	-

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Note 1:
ESM's terms of trade require payment within 30 days of invoice date for both initial payments and final installations.

Note 2:
Other payables include payroll tax payables to the Inland Revenue Board (IRB) which has been outstanding for half a year. Upon negotiation between ESM's finance director and IRB, ESM is permitted a delayed payment with a condition that ESM must pay all its future tax liabilities in year 2023 when they fall due, without any failure.

On top of that, Alya has noted that Dato' Rajes, the managing director who started the business 30 years ago, injected RM1.5 million cash as an interest free loan in order to improve the company's cash flow and reduce the risk to the company of breaching its loan covenant, which is based on interest cover.

Alya has also attached to the audit strategy a recent press cutting describing an accident in July 2023 involving one of ESM 's employees. The employee died after falling through a fragile roof while installing a solar system at the premises of one of ESM 's customers. The incident is being investigated by the health and safety regulator to ascertain whether ESM was in breach of the health and safety regulations with which the company is required to comply. All work has been suspended on that contract until the investigation is completed.

Required:

(a) Justify why the item listed in the audit strategies have been identified as key areas of audit risk and for each item, describe the procedures that should be included in the audit plan in order to address each risk. You should present your answer using two (2) columns format with the following subheadings:

1. Revenue
2. Work in progress
3. Trade receivables
4. Going concern

(24 marks)

(b) Explain why it is important for the external auditor to consider whether ESM has complied with health and safety regulations. (4 marks)

(c) Outline how you should use analytical procedures when reviewing the financial information and state the limitations of using analytical procedures. (4 marks)

(Total: 32 marks)

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QUESTION 3

The following situations have recently been referred to your firm's ethics partner by other partners in your firm.

Emaar Berhad (Emaar)

Your firm is the external auditor for Emaar, a Malaysian listed company. In addition to the external audit, your firm provides recurring non-audit services that are permitted under the ethical standard. Your firm expects to earn the following fees from Emaar in year 2023:

Audit services	Non-audit services
RM'000	RM'000
1,605	920

Your firm's total annual fee income in 2023 is expected to be RM28 million.

Eaton Sdn. Bhd. (Eaton)
Emma is the audit engagement partner for the external audit of Eaton. David, Emma's father, has recently been appointed as Eaton's chief executive.

Jumeirah Group Berhad (Jumeirah)
The audit engagement partner has discovered that during the external audit of Jumeirah, for the year ended 31 December 2022, the audit manager of the engagement team accepted an expensive watch as a gift from Jumeirah for his hard work during the audit. The auditor's report for the year ended 31 December 2022 has been published.

Al-Fardan Sdn. Bhd. (Fardan)
Fardan is a specialist scientific research company. Its directors have requested that your firm accepts an engagement to audit Fardan's financial statements for the year ending 31 August 2023. Fardan recently submitted a loan application and its bank requires a copy of the auditor's report before it decides whether to provide the loan. Fardan's finance director has also requested that your firm provides assistance with the preparation of some aspects of the financial statements.

Required:

Identify and explain the threats to objectivity and independence, and the professional issues (if any), arising in each of the situations above. State any actions that your firm should take in respect of this matter.

(18 marks)

(Total: 18 marks)

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QUESTION 4

Described below are situations which have arisen in respect of two unrelated external audit clients of your firm. The year end in each case is 31 December 2022.

Hayaki Berhad (Hayaki)

The management of Hayaki has refused to provide written representations that:

- it has provided the auditor with all the relevant information and access as agreed in the terms of the audit engagement; and
- all transactions have been recorded and reflected in the financial statements.

Venus Berhad (Venus)

On 23 January 2023, Venus received a letter from the administrator of Permai Berhad (Permai), a customer of Venus. The letter notified Venus that Permai had gone into administration on 17 January 2023. At 31 December 2023, Venus had an amount due from Permai of RM190,000 for goods supplied. The directors of Venus have refused to make any allowance against the amount due from Permai as they are hopeful they will be able to recover the full amount. On examination of Permai' financial statements you have identified that its assets are insufficient to meet the amounts owed to creditors.

Venus's draft financial statements for the year ended 31 December 2022 show a profit before tax of RM1.5 million and total assets of RM8.7 million.

Required:

(a) Explain the key purposes of obtaining written representations from management as part of an external audit engagement. (4 marks)

(b) For each of the two situations outlined above, state whether you would modify the audit opinion. Give reasons for your conclusions and describe the modifications, if any, to each auditor's report.

(10 marks)

(Total: 14 marks)

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QUESTION 5

Your firm is the external auditor of Burj Qalif Bhd (BQ) for the year ended 31 May 2023. The audit fieldwork has been completed. The engagement partner, Mohamad, is performing a review of the audit files and BQ's draft annual report, including its financial statements.

Mohamad made the following observations during his review:

1. The audit work on subsequent events included a review of the minutes of BQ's board meetings held since 31 May 2023. The audit senior highlighted that in the February board minutes, there was discussion about a formal complaint from one of BQ's largest customers. The customer claimed that BQ had failed to meet its contractual obligations.

2. The audit team performed a data analytics routine on journal entries. This highlighted that 18 journals were processed outside of normal office hours.

3. The audit documentation in relation to trade payables notes that BQ did not perform any supplier statement reconciliations during the year.

4. The audit working papers on the human resource cycle further notes that references are not obtained for all new employees of BQ.

On another discussion, BQ's director has requested your firm to review the financial statements of their new subsidiary, name Burj Junior Sdn. Bhd. (BJ) for the year ending 30 September 2023.

Required:

(a) Describe the additional steps Mohamad should take in respect of his observations listed as (1) and (2) above before concluding his review of the BQ audit. For each step, provide the relevant reason.

(6 marks)

(b) In respect of observation (3) and (4), outline the possible consequences of the internal control deficiencies and provide recommendations to remedy the deficiencies.

(6 marks)

(c) Explain how and why the level of assurance provided by an audit firm might differ for a statutory audit and other assurance engagement.

(4 marks)

(Total: 16 marks)

End of Paper